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COMMONWEALTH OF VIRGINIA

STATE CORPORATION COMMISSION

AT RICHMOND, June 7, 1999

JOINT PETITION OF

CASE NO. PUA980050

AQUASOURCE UTILITY, INC.,
CHARLES S. VERDERY,
AND
SYDNOR HYDRODYNAMICS, INC.

For approval to acquire control of
Sydnor Hydrodynamics, Inc.

ORDER GRANTING APPROVAL

On December 18, 1998, AquaSource Utility, Inc., (“AquaSource”, the “Company”), Charles S. Verdery (“Verdery”), and Sydnor Hydrodynamics, Inc. (“Sydnor”), (collectively the “Petitioners”) filed a joint petition under the Utility Transfers Act requesting approval for AquaSource to acquire from Charles S. Verdery all of the stock of Sydnor and Sydnor’s small water company subsidiaries. The Petitioners request, in the alternative, that, if the Commission determines that it lacks jurisdiction in this matter, it issue a declaratory order to that effect.

On February 12, 1999, the Commission issued its Order Extending Time For Review through June 16, 1999.

On May 18, 1999, the Petitioners filed supplemental information amending their joint petition. The Petitioners state that, on March 24, 1999, the Board of Supervisors of James City County (the “County”), authorized the County to acquire by condemnation, all of the water systems owned by Sydnor in that County; specifically, the three- (3) water systems in the First Colony, Indigo Park/White Oaks, and Old Stage Manor subdivisions. The three- (3) water systems comprise approximately 518 customers as compared to more than 10,000 connections involved in the purchase detailed in the original joint petition.

The Petitioners state that Sydnor, under threat of condemnation by the County, is in negotiation with the County for sale of the water systems. If such negotiation fails to result in an agreement to sell the water systems to the County, the County will continue with condemnation proceedings.

AquaSource Utility, Inc., is a wholly-owned subsidiary of AquaSource, Inc., which is, in turn, a wholly-owned subsidiary of DQE, Inc., a publicly traded utility holding company. In addition to water and wastewater utilities, AquaSource and AquaSource, Inc., also own non-regulated water and wastewater related businesses such as construction and engineering companies, water and wastewater system leasing and fabrication businesses, and contract operation services for other owners of water and wastewater facilities.

AquaSource and AquaSource, Inc., (the “Companies”) received approval from their Boards to invest over \$200 million in water and wastewater utility companies. The Companies provide potable water and wastewater services to more than 300,000 customers and are currently negotiating to acquire numerous additional water utilities

across the country, including Virginia. AquaSource is headquartered in Houston, Texas and has several other offices in various areas of the country.

DQE, Inc., the parent company of AquaSource, Inc., is a Pennsylvania based energy service company and parent of Duquesne Light Company, a regulated electric utility providing service in Pennsylvania. DQE, Inc., has assets of more than \$4.6 billion and annual revenues in excess of \$1.2 billion. AquaSource and AquaSource, Inc., report their financial data on a consolidated basis with DQE, Inc.

Verdery owns all the stock of Sydnor. Sydnor is a Virginia general business corporation operating water systems pursuant to Section 13.1-620 (G) of the Code of Virginia. It also operates an unregulated water company and owns five subsidiaries that are small water companies regulated by the Commission pursuant to Chapter 10.2:1 of Title 56 of the Code of Virginia.¹ The five subsidiaries provide service in the counties of Spotsylvania, Powhatan, Caroline; Goochland, Lancaster, Richmond; Isle of Wight, Northumberland, Westmoreland; Essex, Charles City, and New Kent, and the City of Suffolk. Sydnor provides water service in the counties of Culpeper, Cumberland, Essex; Fluvanna, Goochland, Hanover; Henrico, James City, King William; Lancaster, Mathews, Middlesex; Northumberland, Powhatan, Spotsylvania; Westmoreland and York.

AquaSource proposes to purchase, and Verdery proposes to sell to AquaSource, all the stock of Sydnor. As stated in the joint petition, upon consummation of the transaction, Sydnor and its small water company subsidiaries will become a wholly-

¹ Ellerson Wells, Inc., is an unregulated water company that has been in operation since 1952 and which also operates pursuant to § 13.1-620(G). The five small water company subsidiaries are: Alpha Water Corporation, Sydnor Water Corporation, Powhatan Water Works, Inc., James River Service Corporation, and Caroline Utilities, Inc. Caroline Utilities, Inc., provides wastewater services as well as water service.

owned subsidiary of AquaSource and will continue to operate as separate companies. Additionally, AquaSource or AquaSource, Inc., will provide, either directly or under contract with others, certain services to Sydnor and its subsidiaries.

The Petitioners note that, in response to a petition by the customers of Sydnor's First Colony Water System in James City County ("First Colony System"), the Commission asserted jurisdiction under § 13.1-620 G over that water system. Sydnor's First Colony System involves approximately 255 residential customers out of approximately 7,800 customers served by Sydnor's non-regulated water systems. Pursuant to a Commission Order issued on March 3, 1999, in Case No. PUE960133, the Commission retained jurisdiction over the rates and services of that system for a period of at least two- (2) years from the date of that Order.

As represented by AquaSource, small water companies regulated by the Commission pursuant to the Small Water or Sewer Public Utility Act are subject to § 56-88.1 of the Code pursuant to § 56-265.13:7 A. Although there is no contemplated change in the direct ownership of Sydnor's five small water company subsidiaries, the transfer of control of Sydnor constitutes an indirect change in control of its small water subsidiaries and is therefore subject to § 56-88.1 of the Code of Virginia.

AquaSource represents that adequate service at just and reasonable rates will not be impaired or jeopardized by the proposed transfer of control of Sydnor. AquaSource further represents that AquaSource's purchase of Sydnor will serve to maintain stable rates, facilitate capital improvements, and provide access to reasonably priced capital. AquaSource states, in its joint petition, that the acquisition of Sydnor by AquaSource will provide Sydnor access to substantial operating and financial resources. Company states

that, as part of a larger company with a publicly traded parent, Sydnor will have access to less expensive public capital markets to finance future capital improvements to its plant and equipment. AquaSource represents that, after the transaction, the Commission will retain regulatory authority over Sydnor's small water company subsidiaries under Chapter 10.2:1 of Title 56 of the Code of Virginia.

On May 21, 1999, Staff filed a report detailing the results of its investigation. Staff recommends approval of the joint petition, as amended, subject to the following conditions. First, Sydnor should, in the future, be required to create separate legal entities when acquiring or constructing systems. Second, Sydnor should be required to make application for a certificate of public convenience and necessity for the Lake Shawnee system within 30 days of the final order in this case. Staff also recommends that the Petitioners be required to implement certain filing requirements.

In a letter filed on June 3, 1999, counsel for the Petitioners submitted comments on the Staff report. The Petitioners state that they do not object to the granting of approval subject to the conditions recommended by Staff, as clarified and modified in their comments.

The Petitioners state that, based on conversations with Staff, it is their understanding that the condition requiring Sydnor "to create separate legal entities when acquiring or constructing systems" was intended to apply, in the future, to separate systems constructed or acquired with the intention of serving more than 50 customers. The Petitioners also note that such systems should be separately certificated. The Petitioners request that the condition for the filing of the application for certification of the Lake Shawnee system be modified to require the filing of such application within 30

days of the closing of the transaction rather than within 30 days of the final order in this case. The Petitioners note that Staff has no objection to that modification.

THE COMMISSION is of the opinion that the transfer of the stock of Sydnor and Sydnor's small water company subsidiaries requires our approval pursuant to the Utility Transfers Act. Having considered the joint petition, as amended, and representations of the Company and having been advised by Staff, the Commission is also of the opinion and finds that the above-described transfer of control will neither impair nor jeopardize the provision of adequate service to the public at just and reasonable rates. We will grant approval of the joint petition, as amended, subject to the conditions recommended by Staff, as clarified and modified by the Petitioners in their comments. Accordingly,

IT IS ORDERED THAT:

1) Pursuant to §§ 56-88.1 and 56-90 of the Code of Virginia, AquaSource Utility, Inc., is hereby granted approval to acquire control of Sydnor Hydrodynamics, Inc., under the terms and conditions, as clarified and modified herein.

2) Pursuant to §§ 56-88.1 and 56-90 of the Code of Virginia, AquaSource Utility, Inc., is hereby granted approval, to indirectly, acquire control of Sydnor's regulated subsidiary small water companies.

3) The approval granted herein is conditioned upon the following:

- a. Sydnor Hydrodynamics, Inc., shall, within 30 days of the closing of the transaction described herein, file an application for a certificate of public convenience and necessity for the Lake Shawnee Water System; and

- b. Sydnor Hydrodynamics, Inc., shall create a separate legal entity and seek certification for any separate water system that it constructs or acquires in the future if such system is intended to serve more than fifty- (50) customers.
- 4) The approval granted herein shall have no ratemaking implications.
- 5) Sydnor Hydrodynamics, Inc., shall file a Report of Action with the Director of Public Utility Accounting of the Commission on or before August 10, 1999, subject to extension by the Commission's Director of Public Utility Accounting. Such report shall contain the date of transfer, the sales price, and all accounting entries reflecting the transfer.
- 6) Any excess earnings resulting from operational efficiencies or cost reductions shall be at issue in any filings or proceedings addressing rates.
- 7) The approval granted herein shall in no way be deemed to include the recovery of any portion of the consideration paid in excess of the rate base, at the time of closing, through either an acquisition adjustment or any other type of adjustment for ratemaking purposes.
- 8) There appearing nothing further to be done in this matter, the same be, and it hereby is, dismissed.